

VERIZON MASSACHUSETTS

STATE OF MASSACHUSETTS

TESTIMONY

OF

PAULA L. BROWN

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Q. Please state your name and business address.

A. My name is Paula L. Brown. My office is located at 185 Franklin Street, Boston, Massachusetts. My current position is Vice-president – Regulatory.

Q. Please describe your educational and professional background.

A. I received my Bachelor of Arts Degree in Political Science from Vassar College, Poughkeepsie, New York, in 1970. I began my career in the telecommunications industry in June of 1970, when I joined the Commercial Department of New England Telephone ("NET"). I held various positions of increasing responsibilities in that department until 1980, when I was assigned to the Marketing Department. In that department, I was responsible for the operations associated with sales channels. In 1983, I transferred to the Revenue Matters Department where I held various positions associated with pricing access services. From 1984 to 1986, I was assigned to the NYNEX Service Company, which provided services to both NET and New York Telephone Company ("NYT"). When at the Service Company, I worked on federal access service issues. In 1987, I returned to NET and assumed responsibility for planning, pricing, and implementation activities for state access services. In 1989, I was assigned as a Director of Regulatory issues for Massachusetts and the New England states. In 1995, I transferred to the State Regulatory Planning organization and assumed responsibility for pricing issues in New York and the New England states. My responsibilities in that organization were expanded in February 1998, to include all regulatory policy and planning issues. In July of 2000, I assumed my current position and am responsible for regulatory policy and planning for most of the former Bell Atlantic area.

I have testified before the Department on numerous occasions concerning intrastate access pricing, cost issues, and regulatory policy issues. I have also testified before regulatory agencies on similar matters in Maine, Vermont, Rhode Island, and New York.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to present Verizon Massachusetts' ("Verizon MA") proposal for an alternative regulatory plan in response to the Department's *Vote and Order* of February 27, 2001. My testimony begins with a brief review of historical policy goals of the Department and the sweeping regulatory and market changes in the telecommunications industry in Massachusetts over the past several years. I then describe how these changes affect the fashioning of components for an appropriate regulatory plan for Verizon MA. Finally, I describe the specifics of Verizon MA's proposal.

I. MARKET CHANGES AND ITS IMPACT ON REGULATION

Q. Has the Department addressed how changing market conditions can affect the way it regulates the telecommunications industry?

A. Yes. In its examination of telecommunications regulation in 1985 following the AT&T divestiture and in subsequent cost and rate investigations, the Department established economic efficiency, earnings stability, fairness, simplicity, continuity, and universal service as its primary policy and rate design goals for the telecommunications industry. *New England Telephone*, D.P.U. 1731, at 19, 24 (1985), *New England Telephone*, D.P.U. 86-33-G, at 383-384 (1989), *New England Telephone*, D.P.U. 89-300, at 11-15 (1990). In order to further those goals, the Department adopted a regulatory policy of promoting competition in the telecommunications market. The Department found that the introduction of competition in the Commonwealth would enhance the efficiency of the industry and would be beneficial in providing customers with a greater variety of services and in giving all companies an incentive to keep their rates as low as possible. D.P.U. 1731, at 25. The Department noted that competition in markets would obviate the need for regulation of the industry, but determined that because New England Telephone possessed market power at the outset of competition, the policy goals of economic efficiency, fairness and universal service could be jeopardized unless the Company remained subject to traditional regulatory controls, such as rate-of-return and pricing regulation. *Id.*, at 67-68. However, even as early as the mid-1980's, the Department recognized that the unprecedented technological changes that were occurring in the telecommunications market in Massachusetts made it one that was in transition to a competitive market. For this reason, the Department chose to encourage

new entrants by subjecting them to few regulatory constraints, *i.e.*, the minimum statutory requirements. *Id.*, at 63-64. The Department also found that where competition penetrates into a market, it would change the extent of regulation over the Company.

Q. How has the Department implemented the policies it adopted in 1985?

A. Since 1985, the Department has been consistently guided by its policies of furthering competition and adapting its form of regulation to reflect changing circumstances in markets. One of the most significant efforts undertaken by the Department was its comprehensive rebalancing of Verizon MA's rates in D.P.U. 89-300 to better align prices with their underlying costs, thereby producing a rate structure that would reflect competitive markets. The principal changes made by the Department were to substantially lower usage charges (local, toll, and access) while increasing Dial Tone Line rates for business and residence customers. The Department determined that competition would benefit by moving prices toward more economic rate levels and balanced that objective with its concern for rate continuity. To minimize customer impacts as rates were adjusted, the Department determined that rate changes should occur gradually through a series of annual transitional filings.

In other rulings, the Department continued to promote competition by relaxing its regulatory requirements over both the Company and other carriers. For example, in D.P.U. 91-79, the Department found that multiple services offered in the Commonwealth by AT&T "did not require direct price regulation to ensure that the rates for these services are just and reasonable." *AT&T Communications of New England, Inc.*, D.P.U. 91-79, at 56 (1992). In 1994, the Department eliminated the requirement that carriers obtain a certificate of public convenience and necessity from the Department before offering intrastate service in Massachusetts. *Regulatory Treatment of Telecommunications Common Carriers*, D.P.U. 93-98, at 12 (1994). In 1995, the Department adopted a price-cap form of regulation for the Company because it simulated the competitive outcome better than rate-of-return regulation. However, the Department recognized that a price cap form of regulation was only a transitional mechanism and was not appropriate for a fully competitive market because "if effective competition exists, no rate regulation whatsoever ([rate of return], price caps, *etc.*) would be needed...[because] [i]n a competitive market, competition itself will lead to the efficient outcome." D.P.U. 94-50, at 113 (1995). Finally, in 1996, it eliminated price-cap regulation for AT&T's intrastate services, and permitted market-based pricing for all such services. *AT&T Communications of New England, Inc.*, D.P.U. 95-131, at 9 (1996).

Q. What is the current state of competition in retail telecommunications markets in Massachusetts?

A. As described in detail in the testimonies of Mr. Mudge and Dr. Taylor, the Telecommunications Act of 1996 (the "Act") has dramatically and permanently altered the retail markets for telecommunications services in Massachusetts. Both facilities-based CLECs and Resellers are operating in Massachusetts, and the competition for retail consumers is spirited. Dr. Taylor discusses how in this changed market Verizon MA no longer holds the preeminent market position at the retail level. As noted in Dr. Taylor's testimony, the Company's position in markets has been radically changed because: no barriers to competitive entry exist; competitive suppliers are present and active; and competitors have complete access to the market with no substantial investment requirements.

As Mr. Mudge testifies, the telecommunications industry in Massachusetts is one of the most competitive in the nation, with carriers providing competition through resale, unbundled network elements ("UNEs"), and through their own facilities.

Q. Should a new regulation plan for Verizon MA reflect the current competitive market?

A. Yes. When the Department adopted the Price Cap Plan, it stated that, although the plan was appropriate in a market that was moving toward more competition, price-cap regulation was not appropriate for a market exhibiting the presence of effective competition. The Department reiterated that if there is sufficient competition, market-based pricing would replace rate regulation by the Department. D.P.U. 94-50, at 113-115 (1995). Since that time, the market has continued to evolve, and significant changes have taken place as a result of the continuing growth of competition and the implementation of the Act. In light of these changes, Verizon MA is proposing a new alternative regulation plan that recognizes the new competitive marketplace. Verizon MA's proposal represents a further step toward full market-based price regulation, while still providing safeguards to ensure that the Department's telecommunication policy objectives continue to be met.

Q. How has the Act affected the retail market and the appropriate approach to price regulation in Massachusetts?

A. As Mr. Mudge and Dr. Taylor testify, the Act imposes a number of requirements on Verizon MA to ensure that a competitive structure exists in telecommunications markets. Because full facilities-based competition may take some time to develop in all markets and in all areas, the Act requires Verizon MA to offer UNEs at regulated rates to its competitors

and to provide retail services for resale at prescribed discounts. As described by Dr. Taylor, these elements of wholesale rate regulation have important implications on the need for and the form of price regulation for tariffed services in Massachusetts.

Q. How does the requirement for UNE pricing and resale discounts affect the form of price regulation in Massachusetts?

A. The requirements that Verizon MA provide UNEs at Department-approved, cost-based rates and provide retail services at discounted rates to competitors ensures that competition can exist anywhere in the Commonwealth. There is no need for a competitor to build facilities in a geographic area or for a market segment in order to provide service. Competitors are able to compete for any customer to which Verizon MA is able to provide service. The implication of this structure is that Verizon MA faces retail competition for every customer in Massachusetts and, therefore, consistent with the Department's longstanding policies, neither traditional rate-of-return regulation nor price-cap regulation is required for retail services offered by Verizon MA. In essence, the Company's wholesale rates continue to be regulated by the Department based on costs, and Verizon MA's retail rates are effectively regulated by market-based competition.

Q. Does this mean that Verizon MA is proposing market-based pricing for all of its retail intrastate operations?

A. No. Although Department precedent would permit market-based pricing for all retail offerings, Verizon MA's proposed alternative regulation plan (the "Plan") stops short of full market-based pricing at this time. As described below, the Plan is designed to provide continued regulatory protections for the pricing of residential services and for the level of service quality provided to all customers.

II. DESCRIPTION OF THE ALTERNATIVE REGULATION PLAN

Q. Please summarize the basic components of the Plan.

A. The Plan, which is presented as a stand-alone document in this filing, groups services into four categories with different levels of pricing flexibility. For services subject to market-based pricing, the Plan permits full pricing flexibility. For all other services, the Plan provides safeguards, which limit or prohibit price increases. The services are grouped as follows:

1. Services with rates capped for three years. This category includes residence exchange and residence local usage offerings.
2. Services with pricing restricted by revenue neutral filings. This category includes all other residence services.
3. Services subject to market-based prices. For all other services, with the exception of access services, Verizon MA will be permitted to change rates based on market conditions.
4. Services with unique pricing regulations. Existing Department rules will continue to govern services with unique pricing requirements, (*e.g.*, rates for pole and conduit attachments and late payment charges).

Although Verizon MA believes that all retail markets are now subject to effective competition, it understands that there may be some question as to whether all residential customers have full and immediate access to competitive alternatives. In order to address any concerns that market forces are not present to "regulate" prices for particular residential markets, the Plan permits Verizon MA to increase prices for basic residential services in only limited circumstances. In addition, there will be an overall cap on the aggregate rates for other (non-basic) residential services, *i.e.*, any increases in individual service element(s) must be offset by reductions in other residential service elements. Appendix A of the Plan lists all services by category.

Q. What basic residential services will not be increased under the Plan, except in limited circumstances?

A. Except for the circumstances described below, Verizon MA will not increase rates for the Residence Dial Tone Line or Residence local usage services for at least the first three years (Paragraph B of the Plan). However, at the initiation of the Plan, Verizon MA proposes to eliminate the charge for Touch Tone service and to collect those revenues in the Residence Dial Tone Line rate on a revenue-neutral basis (Paragraph A of the Plan). This will increase the Dial Tone Line rate by \$0.47 (see Attachment I to my testimony) from \$9.91 to \$10.38. Concurrently with the increase in Residence Dial-Tone Line, Verizon MA proposes to increase the Lifeline Credit by 47 cents to ensure that eligible Lifeline customers not previously paying for Touch Tone service are not adversely affected by the change.

Q. Why is the Company proposing to eliminate the separate Touch Tone charge for residence customers?

A. Verizon MA is proposing to eliminate the separate Touch Tone charge because the service has become a part of basic service to the vast majority of our customers. Over 90 percent of residence subscribers purchase the feature. Verizon MA eliminated the business charge for Touch Tone service in January of 2000.

Q. Are there any circumstances under which Verizon MA could increase rates for basic residence services during the term of the Plan?

A. Yes. Residence Dial Tone Line and local usage rates could be increased or decreased during the term of the Plan to reflect the impact of exogenous events (Paragraph E of Plan). This provision continues the exogenous adjustment that was included in the Price Cap Plan, approved by the Department in D.P.U. 94-50. As with the Price Cap Plan, any price adjustment to reflect an exogenous event would require Department review and approval.

Q. Are the price changes for "all other retail services" limited under the plan?

A. No. Under Verizon MA's proposed Plan, the market would prescribe price changes for "all other retail services". Verizon MA would be permitted to adjust its rate levels for all other services in response to market conditions. The Company would be allowed to change those rates, subject only to a showing that proposed rate changes meet the Department's price floor rules. Appendix A of the Plan also lists the services that fall into this category.

Q. Please describe the treatment of new services under the Plan.

A. As described in the Plan, new products and services filed by Verizon MA will be subject to the same pricing rules as "all other retail services", *i.e.*, Verizon MA will have pricing discretion over those services subject to the Department's price floor rules. This provision is consistent with the overall regulatory framework of the Plan, which provides Verizon MA with the ability to react quickly to marketplace changes.

Q. What is Verizon MA's proposal for the services that have unique pricing requirements today, such as late payment charges or conduit fees?

A. The mechanisms for setting the level of late payment charges and attachment for poles and conduit established in D.P.U. 93-204-A and D.P.U. 91-218, respectively, also will remain in effect.

Q. What assurances are there that existing prices are at a reasonable level to transition to market based pricing?

A. The Department found that the Company's rate levels were reasonable in D.T.E. 94-50, and since that time, those rates have been under various price cap restrictions that, by definition, guaranteed they change only in accordance with the Department's rules. As a result, the rates and charges have continued to be maintained at reasonable levels.

Q. Verizon MA's proposal eliminates the indices that regulate prices under the previous pricing plan. Why is this proposal better suited to the current market place?

A. As Mr. Mudge and Dr. Taylor testify, the marketplace in Massachusetts has changed dramatically over the last five years following enactment of the Act. Barriers to entry have been removed, and Verizon MA is meeting its obligations under the Act to provide competing carriers with interconnection, UNEs, and resold services. As a result, competition exists throughout Massachusetts in all markets. Given the change in the marketplace, a price cap plan that dictates pricing changes rather than permitting the market to drive price changes, no longer furthers the Department's policies. As explained by Dr. Taylor, continuation of the previous pricing plan distorts and negatively affects competitive forces in the marketplace. Verizon MA's proposed Plan addresses the change in the market by permitting pricing flexibility for all retail services, with the exception of residence services. For residence services, Verizon MA has taken a very conservative approach and proposed safeguards that ensure pricing stability for basic residence exchange services for the next three years. After that period, any change to permit more flexibility in residence prices would require Department approval.

III. ALTERNATIVE PLAN PROVISIONS FOR ACCESS CHARGE REFORM

Q. Has Verizon MA considered possible changes to switched access services?

A. Yes. In its *Vote and Order* opening this proceeding, the Department directed Verizon MA to address "a plan for intrastate access charge reform similar to that approved by the Federal Communications Commission ('FCC') for interstate charges." Although Verizon MA does not believe that a change from the current pricing levels is necessary at this time, it has designed alternative provisions that could be incorporated into the Plan to effectuate such intrastate access charge reform. The alternative provisions, which constitute a revenue-neutral implementation of access-charge reform, are indicated in bold and brackets in the Plan.

Q. Why isn't it necessary to reduce switched access charges at this time?

A. Although Verizon MA supports the gradual movement of usage prices toward economically efficient levels, it recognizes the goal of achieving economically efficient prices must be balanced with other public policy objectives. Currently, both switched access and toll rates contain levels of contribution that ensure lower residence exchange rates. As Dr. Taylor explains, the levels of contribution in switched access rates and toll rates, although perhaps not ideal from an economic perspective, are not inhibiting competition in the residence toll market. Therefore, there is no immediate competitive requirement to reduce intrastate switched access charges to the interstate switched access charge levels. In fact, facility-based CLECs may benefit from switched access charges with higher levels of contribution, because they, too, can use that contribution to offset the expenses associated with providing local exchange service.

Q. Putting aside the concerns that you express, what are the alternatives that you present to restructure intrastate switched access rate elements and reduce the intrastate switched access charges to the interstate levels?

A. There are two alternatives for the reduction of switched access to the current interstate rate levels and rate structure. The first alternative is a flash-cut approach, which reduces the intrastate switched access charges to the interstate structure and rate levels upon implementation of the Plan. This approach produces an increase in the Residence Dial Tone Line of \$1.63 (see Attachment I to my testimony). The second alternative phases-in the reduction of switched access rate levels over a two or three year period. The resulting rate increases to the Residence Dial Tone Line charge is approximately either one half or one third of \$1.63 in each year, respectively. The Plan describes the flash-cut approach and the language would be modified as needed to reflect either alternative.

Q. Please provide an overview of the switched access restructure.

A. The current intrastate switched access rate structure consists of three major categories of charges - Carrier Common Line, Local Switching, and transport. To restructure intrastate access to the current interstate structure, some rate elements are eliminated and others are further unbundled. In particular the structural differences can be grouped as follows:

1. The Carrier Common Line rate element and the Interconnection Charge that provide contribution in today's rate structure are eliminated.
2. The Local Switching rate element is unbundled into a port charge and local switching charge. The port charge is divided into either a measured or flat-rate offering that makes the port structure consistent with the transport structure selected by the carrier. If a carrier selects a

dedicated structure to an end office for transport, it is likely to pay less under a flat-rate structure for the port. In the alternative, if the carrier chooses tandem routing for transport, it is apt to benefit from a measured-rate structure for the end office port charge.

3. The local transport structure, which is currently provided on a dedicated or tandem-routed basis, is further unbundled. When a carrier selects tandem routing, the carrier can subscribe to only the transport elements needed to complete its transport. This structure permits a carrier that collocates to eliminate payment for elements of the former tandem transport structure that they do not use.
4. Finally, the present time-of-day rate structure is eliminated.

Q. Are there any interstate rate elements that are not included in the state rate structure?

A. Yes. The alternative provisions would mirror the current interstate switched access rate structure, with the principal exception of the interstate Primary Interexchange Carrier Charges ("PICCs"). Verizon MA is not proposing PICCs for the intrastate rate restructure in Massachusetts, because in the interstate jurisdiction, this element is either charged to the end user or flowed through to the end user via rates. Given Verizon MA's proposal to implement a revenue-neutral change to the Residence Dial Tone Line rate, there is no reason to establish a separate PICC-like rate element to flow through to the end user in the intrastate jurisdiction.

Q. What is the rate reduction associated with the change to the interstate rate levels and rate structure?

A. The movement of state switched access to the interstate rates and rate structure reduces the overall intrastate switched access rate per minute of use ("MOU") in Massachusetts, from approximately \$0.039 per MOU to \$0.0125 per MOU on an end-to-end basis. The proposed rate levels and structure for switched access services are detailed in the Attachment II to my testimony. Included in that attachment is a detailed description of the rate structure changes, a comparison of the present and proposed average rate per minute, and diagrams that compare the current and proposed rate structures.

Q. Under the alternative provisions of the Plan, when would Verizon MA implement the switched access changes?

A. Verizon MA would reduce and restructure intrastate switched access rates 75 days after the effective date of the Plan. Alternatively, as indicated previously, the Company could accomplish this rebalancing of

rates over two or three years with proportionate annual reductions in the access charges.

Q. What impact would the change in intrastate access charges have on Verizon MA's other retail rates?

A. The restructuring of intrastate access charges as described above would cause an immediate loss of revenue of \$51.9 million. As part of the alternative provisions of the Plan, Residence Dial Tone Line rate would be increased by \$1.63 to offset the switched access rate decreases on a revenue-neutral basis. This increase is in addition to the \$0.47 resulting from the proposed Touch Tone restructure. If the alternative provisions were implemented, the Lifeline Credit would be increased by \$1.63 to protect eligible customers. As previously indicated, the revenue reduction and Dial Tone Line increase could also be spread over two or three years with corresponding rate offsets to the Lifeline Credit.

Q. Would there be any other rate rebalancing required if the intrastate switched access rates were reduced?

A. Yes. The Department has long recognized the relationship between switched access services and toll services, and in D.P.U. 89-300, linked price changes for the two sets of services. D.P.U. 89-300, at 203-204, 217. The Department continued this linkage in D.P.U. 94-50. D.P.U. 94-50, at 249. The proposed reduction in access rates contained in the alternative provisions of the Plan may require that residence toll and optional calling plan rates be reduced. Verizon MA cannot determine precisely where and when competitors would reduce prices as they flow-through their cost reductions to consumers. Competitors would respond to the marketplace demands, and Verizon MA would also need to adjust its toll prices to meet the competition. In the event that Verizon MA reduces residence toll prices, (including those incorporated in optional calling plans), in response to such competitive pressures associated with the change in access rates, Verizon MA would be permitted, to increase Residence Dial Tone Line rates on a revenue-neutral basis to offset the revenue loss. As a further regulatory protection for customers of basic residence service, the alternative provisions of the Plan would limit the increase in the monthly dial tone rate to a cumulative amount of \$1.00 per Residence Dial Tone Line. Verizon MA is permitted one increase in the Dial Tone Line rate per year and could make such an increase only through the fourth year of the Plan (Paragraph G of the Plan).

Q. What if the residence toll reductions fall short of the \$1.00 per line?

A. The Dial Tone Line rate would increase only to the extent necessary to offset the amount of residence toll revenue reductions.

Q. What if the residence toll reductions resulted in an increase that was greater than \$1.00?

A. The Residence Dial Tone Line increase would be limited to a maximum of \$1.00 in total. Any reductions beyond that fixed amount could only be offset by increases in rates other than the Residence Dial Tone Line. If Verizon MA proposed such increases, they would need to be approved by the Department as part of a revenue-neutral filing.

Q. Why is Verizon MA proposing to offset the access and residence toll reductions with increases to the Residence Dial Tone Line charge?

A. Verizon MA is proposing that the reduction in switched access be offset by an increase in the Residence Dial Tone Line rate to move the rate toward more economically efficient rate levels. This rate movement is consistent with previous Department findings.

Q. In what cases did the Department consider the appropriate pricing of retail services including the Dial Tone Line?

A. The Department laid out the framework for the entrance of competition in D.P.U. 1731, and considered the appropriate costing and pricing of retail services in D.P.U. 86-33 and D.P.U. 89-300.

Q. What did the Department determine in these dockets related to the appropriate pricing of the Dial Tone Line?

A. As I previously noted, the Department conducted an extensive examination of the Company's rates and rate structure following its order in 1985 in D.P.U. 1731 to better align rates with costs to approximate prices that would exist in a competitive market. As part of that multi-year investigation, the Department reviewed both the embedded and incremental costs of Verizon MA and determined that marginal costs represented the most efficient costs to be considered for pricing services as competition entered a marketplace and were consistent with the Department's goals of efficiency and fairness. D.P.U. 1731, at 38; D.P.U. 86-33-G, at 384. The Department also determined that it was not necessary to calculate the marginal cost for the Dial Tone Line because that element "becomes the repository of any residual revenue requirement left over after use related rates are set at marginal costs." D.P.U. 86-33-G, at 464-465.

In D.P.U.89-300, Verizon MA provided numerous Illustrative tariffs which showed a variety of rate designs under which all rates with the exception of the most inelastic rate elements were priced at marginal costs. The Dial Tone Line was identified as the most inelastic rate element in

each scenario where the Dial Tone Line was one of the rate elements in the grouping of rate elements. The most inelastic rate elements in each of the scenarios were residually priced. In its Order in D.P.U. 89-300, the Department found that the Illustrative tariffs were useful to establish the general framework for future rate structure filings, the appropriate direction for future rate changes, and the appropriate magnitude of future changes. The Illustrative tariff rates for the Residence Dial Tone Line range between approximately \$16.00 and \$24.00 depending upon the scenario. The Department found that scenario H, in which the services were grouped by rate class (Residence, Business, Carrier Access and Coin), to be the most instructive scenario. D.P.U. 89-300 at 31-32. Under scenario H, the Residence Dial Tone Line was residually priced at approximately \$22.00.

Q. Did the Department make any other determinations regarding the appropriate pricing of the Dial Tone Line?

A. Yes. The Department also agreed that the proposed target rate level for the residence Dial Tone Line of \$15.00 was a reasonable target rate and indicated that the Department desired to have rates eventually reach the target rate levels. D.P.U. 89-300, at 82-83.

Q. Did the Department determine the timing of rate changes to the target level?

A. Yes. The Department found that an immediate movement to target rate levels would be contrary to its goal of rate continuity. Therefore, the Department ordered a series of transitional filings that moved rates toward the more efficient rate levels. These filings, which were known as the "Transitional" filings, continued the movement of prices toward the more economically efficient levels determined by the Department. In these filings, the prices for wholesale and retail usage services were lowered toward target rate levels (established in D.P.U. 89-300) and the Residence Dial Tone Line charge was residually increased. The Business Dial Tone Line was set at the target rate level in compliance with the Department's Order in D.P.U. 89-300, and therefore was not increased further in the transitional filings.

Q. Was the target rate for the Residence Dial Tone Line achieved?

A. No. In D.P.U. 94-50, the systematic movement of rates toward target rate levels via transitional filings was suspended. Only switched access charges were reduced to the target rate levels. Other retail rates were either capped or became subject to the pricing rules of the Price Cap Plan.

Q. Is Verizon MA proposing to increase the Residence Dial Tone Line to the target rate level in this filing?

A. No. Verizon MA is using the same pricing principles that guided the previous rate rebalancing efforts in the Commonwealth as guidance for the pricing principles that should be used to respond to the Department's request for a proposal to further reduce switched access charges. A reduction in switched access and toll charges is a movement of these rates toward marginal costs. The revenue offset should be placed on the most inelastic rate element, which continues to be the Dial Tone Line.

Q. What is the impact of this proposal on Lifeline customers?

A. As previously indicated, there will be no impact for Lifeline customers because Verizon MA is proposing an increase in the Lifeline Credit equal to the increase in the Residence Dial Tone Line rate.

Q. How will business toll reductions be handled?

A. Under the Plan, Verizon MA will have the flexibility to set prices for all business services based on market considerations, and accordingly, the Company will be at risk for any revenue loss associated with business toll reductions resulting from the lowering of access rates.

IV. OTHER ELEMENTS OF THE PLAN

Q. Does the proposed plan include a component for exogenous changes?

A. Yes. When the Department established the price cap plan it recognized that there were certain changes that were beyond the control of Verizon MA and that Verizon MA should be granted relief from its pricing restrictions should those changes occur. The Plan contains provisions similar to the previous plan.

Q. Is there any difference in the exogenous change provision?

A. Yes. When the previous plan was filed, the word "cost" was intended to include any changes that affected revenues. The language is clarified to avoid any potential confusion and now refers to both costs and revenues.

Q. Does the Plan contain a service quality component?

A. Yes. The Service quality component of the Plan is similar to the existing service quality plan with changes in the application of penalties. The modifications are described in Mr. Mudge's testimony.

V. CONCLUSION

Q. Would you summarize why the proposed Plan is in the public interest?

A. Yes. The Plan:

1. Provides another significant step toward market-based pricing for telecommunication services in Massachusetts;
2. Provides safeguards for residence customers;
3. Provides increased competitive parity by moving prices closer to costs;
4. Allows Verizon Massachusetts some measure of pricing latitude that its competitors already enjoy, while requiring the Company to assume significant competitive risks;
5. Better reflects today's telecommunications environment; and permits the market place to react to competitive offerings and prices; and
6. Provides for continued Service Quality assurance.

The Plan moves the pricing of telecommunication services closer to market-based pricing which should ultimately benefit all consumers in the Commonwealth.

Q. Does this conclude your testimony?

A. Yes.